

# The Big Behavioural Economics Debate

**I**n order to bring alive the practicalities of embracing behavioural economics in market research, I asked each of the four members of the ESOMAR Behavioural Economics Seminar Advisory Board a few of the most common questions that practitioners raise about doing BE-led research.

Their answers reveal some very strong areas of agreement and some very clear shared advice about the practical steps researchers can take. But, as you might expect, there is also some healthy debate about quite how close research practice should be to what goes on in the science.



## Q1. How do you explain BE to clients and colleagues?

Steve: It is the study of human behaviour grounded in real life, not academic assumptions. It helps us understand what real people do in real-life situations.

Caroline: We call it 'decision science.' It helps explain what BE does rather than what it is.

Florian: Until recently, there was no theoretical basis for market research other than the implicit model of the *Homo economicus*. BE changed that and replaced this flawed model with empirically validated

insights into the heuristics and biases of human decision making on the basis of countless experiments.

John: Agreed. *Homo economicus* is as flawed in economics as the left brain/right brain persuasion model in marketing. Better is Kahneman's model which says most decisions are made instinctively, emotionally [System 1] and then post-rationalised cognitively [System 2]. Emotion trumps logic; seduction trumps persuasion.

## Q 2. Is BE a fundamental challenge to everything we do – from surveys to focus groups? Or is it an enhancer of market research?

Steve: To me, it is an enhancer. We should look at our current approaches with a BE lens and decide how appropriate they still are. Some techniques will come through fine; others will be found inappropriate (conjoint being my favourite example of a methodology based on academic assumption and not in any way grounded in real human understanding).

Caroline: Its significance cannot be underestimated. Just as marketing has taught us for the last 20 years that attitude precedes behaviour and thus became the prevailing wisdom of the times, so BE should become the new prevailing wisdom. BE permeates everything we do.

John: BE helps market research answer its two biggest challenges: to provide marketers with a more accurate model of

how people really make decisions and, therefore, how to build famous brands. This means changing what we measure and how.

Florian: BE adds to market research what is urgently missing. It is nothing less than the theoretical basis for everything we do in market research.

### Q 3. What kind of response have you had from clients? Have these responses changed over time?

Florian: At first, it seemed to many like an interesting side issue; today it is supported by many case studies and advanced tools. They accept it as a much more efficient way of doing research, although the level of

acceptance is also very sector specific.

Caroline: We tailor how we use it based on the client. Some like the thinking behind it to be made explicit; some prefer a more implicit approach.

Steve: BE has become a topic of interest and discussion, and our input into the debate has even led to us getting a few more briefs! However, when we talk about our work, we don't necessarily focus on the BE component but instead what the results will do for our client's business

John: The more senior the client, the more they love it and want to introduce it. The conversation then turns to how best to change the culture and introduce it, since it challenges and changes so much.

### Q 4. What mistakes have you made in trying to apply BE to market research practice?

John: Many. The paradox of success is you need failure to achieve it. We continue to experiment to perfect our System 1 suite of research tools and models in market prediction.

Florian: We continuously improve our models and approaches – looking back, we obviously made many mistakes, from which we profited a lot. This is the core of any empirical science and in that sense a feature, not a bug.

Caroline: You have to experiment to move forward, but BE has opened more doors than it's closed. The biggest mistake is pitching it at the wrong level to prospective clients – some think they want the theory but don't have the appetite for it when faced with it. How to engage and excite people is about the storytelling of BE – it shouldn't be overlooked.

Steve: 'The mistake is when you don't apply it, not when you do. Our mistakes have been when we keep going with the traditional technique instead of arguing more forcefully that an approach centred on understanding real-life human behaviour is the way forward.'

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FLORIAN BAUER

## The Art of Pricing with Behavioural Economics

Classic pricing tools implicitly build on the assumption that customers behave like the famous *Homo economicus* - perfectly informed, selfish and rational decision makers with stable preference. Tools like conjoint analysis, price sensitivity measurement and the like ignore a wealth of insights about human decision making. More critically, they are incapable of identifying profit potentials that are hidden beyond people's predictably irrational decisions.

### ENTER BEHAVIOURAL ECONOMICS

This seems to be a wonderful starting point for behavioural economics to fundamentally revolutionise pricing research. To date, the insights from BE add up to an unstructured menu of findings. In this forum, they are not systematically transferable to any specific area of application. A framework is missing that structures the insights from a pricing perspective and helps to leverage them to further develop the classic pricing tools.

One may ask why we need a new research framework, as many insights from BE centre around misconceptions of pricing. If we have to define a pricing strategy for an existing company in a given sector and a specific

product, things become more difficult. The 'psychological price profile' is such a framework (Bauer, 2011a & 2011b). It basically describes the motivational, cognitive and behavioural dimensions we need to better understand in order to derive an optimised pricing strategy. As such, this framework goes far beyond the classic tools, as they only primarily measure price assessment.

### COGNITIVE DIMENSIONS

Let's take a closer look at the cognitive dimensions to illustrate this: If we have to define the maximally acceptable price increase for a newspaper subscription, it is not sufficient to ask for the maximum price which subscribers would accept. To really understand how far a publisher can go, we also have to understand whether subscribers actually know the current price, whether they remember the last price increase (both reflecting price knowledge) and how important price was in comparison to all other decision criteria (price interest). Once we understand all three cognitive dimensions, we can predict the price level up to which we can go without losing circulation. If a subscriber has no clue about the current price level,

we do not need to take much care about his stated willingness to accept a price increase – especially if the price was not a key decision criteria and he is not able to recall the last price increase. We need to cultivate pricing research beyond the measurement of price sensitivity. In addition, applying BE in pricing has taught us some additional lessons:

1. Stop inductive application of BE: For applying BE in market research, we have to get beyond the inductive transfer of isolated experimental results to marketing questions – this will not work more often than it will be successful.
2. BE is about emotion, cognition and behaviour: BE tells us to look at more dimensions than the classic tools can cover. None of them is more important than the other, as the insights emerge from a simultaneous analysis of all dimensions.
3. BE is a conceptual – not methodological – revolution: BE in no way favours any methodological approach (eg, qualitative vs. quantitative); BE is primarily about accepting that humans do not behave like *Homo economicus*; hence, BE primarily focusses on evolving the conceptual framework (Bauer, 2006).

To date, the insights from behavioural economics add up to a rather unstructured menu of findings. In this form, they are not systematically transferable to any specific area of application. A framework is missing that structures the insights from a pricing perspective and helps to leverage them to further develop the classic pricing tools.

### References

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### Q 5. What are the big implications for our practice and our frameworks?

Steve: We need to be doing more research in the context of people's real lives. This means fewer long questionnaires and more bite-sized, mobile pieces of data gathering. We need to change the way we do qual and spend more time observing people in their daily life.

John: Market research needs to stop taking what people say literally and move to observing what they do and measuring how they feel. In particular, we need to move from predominantly measuring people's System 2 post-rationalisations of their attitudes and actions and move to predominantly measuring people's System 1 feelings and instinctive reactions. Why so much emphasis on System 1? Well, first, the systems are not equal, with System 1 having by far the bigger influence on decision making; second, the current traditional measures of System 2 which dominate market research have been, and will continue to be, poor predictors of what has made brands famous and commercially

successful, because they're largely post-rationalisations. An emphasis on System 1 measures will help market research lead in how to build famous brands.

Florian: Reflecting the wide range of BE insights, we need to understand rational and emotional aspects on an unconscious and conscious level. BE is about System 1 and System 2 – and their respective interaction. The key statement of BE is exactly this – a need for a more balanced approach in order to understand decisions holistically. Focussing only on one dimension would mean making the same mistake that we blame traditional research approaches for – just in the opposite direction. The question which one is more important is, firstly, very much dependent on the nature of the decision at hand. Routinely buying washing power is different from trading off different mobile telco tariffs. And issues like branding might be different from pricing. Secondly, the question which one is generally more important is practically irrelevant. It's like trying to answer the question if predisposition or

socialisation is more important for the development of intelligence. Here, scientists gave up answering this question and rather focus on understanding how both determinants interact. This is what market research should do, too.

Caroline: It is helpful across the board and permeates everything we do – from project design to recruitment, pre-tasks, participant exercises, etc. We should ensure enough time for System 1 answers – non-verbal responses, creative exercises, etc. We should recognise System 2 thinking when we see it and keep it in perspective with System 1, rather than asking endless batteries of System 2 questions. Where it falls down is when it meets with loss aversion – a resistance to change, either within the research thinking or in the client organisation.

John: Part of the issue here is creating a usable model of the science relevant to what is being researched. I feel strongly that if we want BE to be adopted and have the impact it should have on research and marketing, then we need to make it as simple as we possibly can without making it simplistic – to quote the famous adage, 'Simplicity is the ultimate sophistication.' Even so, any simplification still needs to be rooted in empirical data and proof, which is very much at the heart of what we're doing.

How can trying to better reflect genuine human behaviour be a passing fad?



It's clearly a matter of balance, but for us, the reward of our simplified models is in the impact we're able to have on famous brand building.

**Q 6. Is it here to stay or is it just a passing fad?**

Steve: How can trying to better reflect genuine human behaviour be a passing fad?

John: It's a better understanding of human behaviour and here to stay. Whether market research embraces it will dictate whether market research thrives or becomes the passing fad.

Florian: Is the fact that the earth is not flat here to stay or just a passing insight?

Caroline: Here to stay. No question.

**Q 7. What's next?**

Steve: The continuing erosion of some traditional techniques and more and more context-based research.

John: Better explanations of behavioural science, better models for applying it, better ways of measuring it, better brand-building results and a vastly improved status for market research.

Florian: Less assumptions, standardised approaches, focus on benchmarks. More focus on the model of choice, longitudinal research, experimental designs, ethnographic approaches, combinations of qualitative and quantitative research, customised research and consulting.

Caroline: Better research, more exciting insight and a real move forward away from 1950s-style marketing. We need to get better at using it, explaining it and pushing the boundaries.

**Q 8. What one piece of advice would you give research buyers and practitioners in making the science useful?**

Steve: Every time you write a proposal, think about the data gathering you are suggesting and ask whether this feels natural.

Florian: Never start with the method, as it is always only a means to an end. Always start with the model of the choice you want to understand and predict.

Caroline: Always start off your thinking by developing hypotheses: what might be at the heart of the behaviour you want to change? These hypotheses should shape everything you do moving forward. They'll give you a sense of focus and yield far richer, more accurate insight. Embrace it.

John: Educate, evangelise, encourage, experiment and establish behavioural science as a superior way to build famous brands.

The big lesson here for all of us is probably this: behavioural economics is not going away anytime soon. Indeed, as time passes, it seems to offer more and more opportunities for different researchers and research businesses. The question is, what you are going to do with it? **RW**



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